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IN THE

Supreme Court of the United States

OCTOBER TERM, 1937.

No. 455

FREDERICK S. DEITRICK, Receiver of the Boston-Continental National Bank, *et al.*,
Petitioners,

v.

STANDARD SURETY & CASUALTY CO. OF NEW YORK,
Respondent.
(And Six Other Actions Consolidated Therewith)

PETITION FOR WRIT OF CERTIORARI.

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FREDERICK S. DEITRICK, Receiver of the Boston-Continental National Bank, *et al.*,
Petitioners,

v.

STANDARD-SURETY & CASUALTY CO. OF NEW YORK,
Respondent.
(And Six Other Actions Consolidated Therewith)

PETITION FOR WRIT OF CERTIORARI.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioners respectfully show to this Honorable Court as follows:

Description of the Parties and Proceedings.

One of the petitioners, Frederick S. Deitrick, is the Receiver of the Boston-Continental National Bank, an insolvent national banking association which was closed by order of the Comptroller of the Currency on December 17,

1931 (R. 44). Said Bank is the other petitioner. The Bank was established in December 1930 by the consolidation of the Boston National Bank and the Continental National Bank. The petitioner Bank was located in Boston in the District of Massachusetts.

The respondent Standard Surety & Casualty Co. of New York is a New York corporation engaged in the business of writing surety and guaranty bonds and other like obligations and conducted its business in Boston through its attorney-in-fact, one Percy G. Cliff, acting under a written power of attorney. The respondent will be referred to as the "Surety Company".

When the bank suspended business it held four so-called "note guaranty bonds" executed by the Surety Company as guarantor in favor of the Bank as obligee, securing the payment of various notes executed by borrowers from the Bank.

The three actions at law were brought by the Receiver upon three of the aforesaid bonds (R. 43).

The four suits in Equity were brought by the Surety Company against the Receiver and the Bank and sought the cancellation and surrender of these several bonds on the ground that the Surety Company's agent acted in fraud of his principal in giving the bonds and his fraud was known to the president of the Bank. The Receiver, in his answers to the bills of complaint in the Equity cases, counterclaimed on each bond (R. 43).

All of the cases were consolidated for trial and the Master and Auditor made a single report, concluding and recommending that the Receiver should recover on three of the bonds (R. 42-129). The cases were consolidated for all purposes of appeal. (R. 146).

In both the United States District Court (R. 139-141) and the Circuit Court of Appeals for the First Circuit (R. 281-289), the Receiver was denied relief in all of the cases and decrees were ordered directing the surrender and cancellation of the several bonds.

The Matter Involved.

The facts as found by the Master and Auditor (R. 42-129) are summarized in the supporting brief submitted herewith. By stipulation the findings of the Auditor are final (R. 27, 139, 282).

The question presented is whether a receiver of an insolvent national bank stands better than the bank itself with respect to the enforcement of obligations (in the instant case the obligations were "note-guaranty bonds") which

(a) were given to the bank, as a part of a scheme to defraud, upon an understanding between the maker thereof (acting through an agent, in the cases at bar) and a fraudulent bank official that the obligations would be used only to exhibit to the national bank examiners and other interested persons so as to give notes secured thereby the appearance of sound and enforceable assets and would be surrendered later to the maker;

(b) were exhibited to the bank examiners and relied upon by them as genuine, with resulting loss to depositors by reason of the consequent concealment of the unsound condition of the bank;

(c) were exhibited to the bank directors and relied upon by them as genuine, with resulting loss to depositors by reason of the consequent concealment of the unsound condition of the bank; and

(d) were executed without known monetary consideration, by an agent of the maker acting in the premises under a written power of attorney of unlimited scope which was likewise exhibited to and relied upon by the bank examiners as proof of the agent's authority in accordance with the intention of the principal that the power should be so exhibited to all persons having occasion to rely upon the agent's signature.

The Circuit Court of Appeals for the First Circuit ruled that the Receiver could not recover upon the obligations,

because (1) a fraudulent officer of the bank (acting in collusion with the promissor's agent in a scheme to defraud the bank) knew that the agent was acting in fraud of his principal; and (2) that such knowledge was to be imputed to the bank; and (3) that under such circumstances the receiver stands no better than the bank itself (R. 281-293).

The Circuit Court of Appeals for the First Circuit recognized the existence of decisions of various state courts to the contrary, but appears to hold the opinion that the rule of law as to the status of a receiver of a national bank, as above stated, is a rule binding on the federal courts because of the decisions in the cases of *Scott* v. *Armstrong*, 146 U. S. 499; 36 L. Ed. 1059; *Fourth Street National Bank* v. *Yardley*, 165 U. S. 634; 41 L. Ed. 855; and *Rankin, Receiver*, v. *City National Bank*, 208 U. S. 541; 52 L. Ed. 610.

Reasons Relied Upon for Allowance of the Writ.

The petitioner submits that:

1. The ruling of the Circuit Court of Appeals (as decisive of the rights of the parties) that a receiver of a national bank stands no better than the bank itself with respect to the enforcement of obligations acquired by the bank prior to receivership involves an important question of law **which has not been but should be settled by this court.**

We will endeavor to show in the brief accompanying this petition that the three decisions of this court relied upon by the Circuit Court of Appeals do not hold as a rule of law that a receiver of a national bank is to be denied recovery on obligations held by his bank merely because the bank itself could not have recovered thereon.

2. The ruling of the Circuit Court of Appeals is in conflict with decisions of this Court recognizing the principle that a receiver of a bank may have rights with respect to third parties superior to the rights of the bank itself. See

Texas and Pacific Railway Co. v. *Pottorff*, 291 U. S. 245. 78 L. Ed. 777, and other cases discussed in the brief accompanying this petition (pp. 17, 18).

3. The question of law here involved has been the subject of conflicting opinions among the several Circuit Courts of Appeals and is one with respect to which there should be a uniform rule in the various Federal courts.

4. The ruling of the Circuit Court of Appeals is in conflict with the weight of authority in that an overwhelming majority of the highest courts of the several states have adopted a position directly contrary to that taken by the Circuit Court of Appeals in the instant case.

5. The question of Federal law decided by the Circuit Court of Appeals is one of substantial public importance, inasmuch as it relates to the broad question of the rights of receivers of national banks in cases where bank officers have conspired with third parties to defraud the bank and its depositors by having obligations, prima facie valid and enforceable, (but intended otherwise by private agreement between the conspirators) given to the bank for the purpose of deceiving the bank examiners and the Comptroller of the Currency, thus enabling the bank to remain open for business when it otherwise would be closed for the protection of its creditors.

Wherefore Your Petitioners Respectfully Pray:

That a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the Circuit Court of Appeals for the First Circuit, commanding that Court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and proceedings in the cases at bar to the end that the judgments and decrees of the Circuit Court of Appeals may be reviewed by this

Honorable Court, and that your petitioners may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

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Respondent.
(And Six Other Actions Consolidated Therewith)

BRIEF FOR FREDERICK S. DEITRICK, RECEIVER, AND BOSTON-CONTINENTAL NATIONAL BANK, PETITIONERS.

Opinions Below

The opinion of the United States District Court is not reported. It appears in the record at pages 139-141.

The opinion of the Circuit Court of Appeals for the First Circuit bears date of June 1, 1937, appears in the Record at pages 279-288, and is reported in 90 F. (2d) 862.

The opinion of the Circuit Court of Appeals for the First Circuit denying a petition for rehearing appears in the Record at pages 291-293 and is reported in 90 F. (2d) 862, 866. The order denying the petition for rehearing was entered June 29, 1937 (R. 293).

Jurisdiction.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of Congress approved February 13, 1925, c. 229, Sec. 1, 43 Stat. 938; 28 U. S. C. 347(a).

Statement of the Case.

The three actions at law (R. 42, 43) were brought in the United States District Court for the District of Massachusetts by John B. Cunningham, as Receiver of the Boston-Continental National Bank, an insolvent national banking association which was closed by order of the Comptroller of the Currency on December 17, 1931, and were prosecuted by successive receivers of said bank, of which the petitioner Frederick S. Deitrick is the last in order of succession and now holds said office. The defendant in each of the actions at law is Standard Surety & Casualty Co. of New York (hereinafter referred to as the "Surety Company"). In these actions the receiver sought to recover on three so-called "note-guaranty bonds" executed by the Surety Company as co-obligor with three separate borrowers from the bank, namely Westchester Discount Corporation, one Stone and one Robinson. The Bank was the obligee in each of the bonds. The bonds purported to guarantee the payment of certain notes of the respective borrowers, all of which proved to be uncollectible.

The four equity cases (R. 42, 43) were brought by the Surety Company against the Bank and its receiver and sought the cancellation of the three note-guaranty bonds above referred to and also of a fourth bond of similar tenor given to secure the payment of the note of one Cronin. In each of the equity suits the receiver in his answer counterclaimed on each of the bonds.

The actions at law were referred to an Auditor and the suits in equity were referred to the same party as Master (R. 26, 27). The cases were consolidated for trial and the

Master and Auditor made a single report (R. 42-129), wherein he concluded and recommended that the Surety Company be held liable to the Receiver on three of the bonds. However, the United States District Court ordered judgment for the defendant in the three actions at law; disallowed the receiver's counterclaim in the suits in equity; and ordered decrees in favor of the Surety Company directing the surrender and cancellation of the bonds (R. 141).

On appeal to the Circuit Court of Appeals the judgments and orders of the District Court were affirmed (R. 288).

By order of the District Court the cases were consolidated for all purposes of appeal (R. 147).

The pertinent facts as found by the Master and Auditor (R. 42-129) are briefly as follows:

Ragan, President of the Boston-Continental National Bank, herein referred to as "Bank", and previously President of the predecessor Continental National Bank, was engaged in a scheme to defraud the banks for his own dishonest ends. For this purpose he enlisted the aid of one, Percy G. Cliff, who was the attorney-in-fact of the respondent Surety Company for the Boston district (R. 45) and duly licensed to conduct its business in the State of Massachusetts (R. 54). The Surety Company had given to Cliff a general and unlimited power of attorney which authorized him to execute and deliver in the name of the Surety Company and under its corporate seal, various kinds of bonds and undertakings, including the type of note-guaranty bonds given as above stated (R. 93-95). The Surety Company furnished Cliff with its corporate seal (R. 54), printed forms, stationery, and other materials suitable for the writing of bonds and other obligations, and gave him multiple originals of his power of attorney, duly certified and authenticated by the officials of the Surety Company (R. 45, 46).

The bonds were executed and delivered by Cliff at the suggestion or request of Ragan, the Bank's President, for

the avowed purpose of exhibiting the same to the bank examiners (R. 45, 104), to the end that the promissory notes given by Cronin, Stone, Robinson and Westchester Discount Corporation (having an aggregate face value of approximately $120,000) might appear to be adequately secured because of the existence of the guaranty bonds (R. 54). Ragan knew that in writing these particular bonds Cliff was violating certain private instructions from his principal (R. 47), although the terms of his power of attorney were sufficiently broad and general to authorize his writing bonds of this type (R. 54). Cliff knew the fraudulent character of his act (R. 54) but his motive for participating in the fraud was not disclosed. However, the surety does not deny that notwithstanding these circumstances the power of attorney was sufficiently broad to cover the type of bond here in question.

It was the intention of the Surety Company that the general power of attorney should be exhibited to persons dealing with Cliff (R. 46). Duplicate originals of the power, furnished by the Surety Company for the purpose, were attached to two of the bonds (R. 46, 49) and were examined and relied upon by the bank examiners as proof of Cliff's authority in the premises (R. 54, 55).

All of the bonds were exhibited to the bank examiners from time to time and were relied upon by them as being genuine (R. 55, 58), with the result that the true condition of the Bank was concealed from the Comptroller and his examiners thus temporarily forestalling vigorous action by the Comptroller of the Currency to protect the depositors and prevent losses to potential new depositors (R. 59).

But for the existence of the note-guaranty bonds and reliance thereon by the directors, bank examiners and Comptroller, the Bank's unsound condition would have been discovered at a much earlier date, and the losses of the depositors would have been minimized (R. 59).

The directors of the Bank were not parties to the fraud and knew nothing of the infirmities surrounding Cliff's

action in executing and delivering the bonds in question. The bonds were exhibited to the directors when the loans in question were under discussion for approval, extension or renewal from time to time (R. 53). Ragan made all of the loans in question without prior consultation with the board of directors, but all of the loans were approved by the board at subsequent dates in reliance upon the bonds and renewals and extensions thereof were likewise approved (R. 53). No officer or employee of the bank, except Ragan, knew of any infirmity in the bonds (R. 53).

At the time each of the bonds was given, Ragan (The Bank's president) assured Cliff (the Surety Company's agent) that the bonds were to be used only as "window-dressing" (R. 49); that they would never be enforced by the Bank; and that they would be returned to Cliff in due time after they had served their purpose of deceiving the examiners (R. 49, 50, 52, 54). It was understood between Cliff and Ragan that Cliff would not report the writing of the bonds to his home office and would not bill any premiums to the principal obligors on the bonds (R. 45). Furthermore, Ragan, at the time each bond was delivered, or shortly thereafter, gave Cliff a written release respecting each bond, which he signed as president of the Bank (R. 47, 50, 52).

The proceeds of three notes secured by three of the aforesaid bonds apparently were used for the actual benefit of persons other than Ragan (R. 44, 50, 51).

The bond given to secure the obligation of the Westchester Discount Corporation in the penal sum of $40,000 was given at the request of Ragan, prior to the consolidation of the Boston National Bank and the Continental National Bank, and Ragan disclosed to Cliff the fact that the money loaned on the note of Westchester Discount Corporation was to be used by Ragan to purchase additional shares in the Boston-Continental National Bank at a time when the merger between the Boston National Bank and the Continental National Bank was under consideration for

the purpose of forming the Bank which is one of the petitioners herein. In connection with this merger the Comptroller of the Currency had insisted that the capital structure of the consolidated bank must be re-enforced by the issue of new stock and Ragan required $40,000 for the purpose of paying his cash subscription for such new stock (R. 49).

When the Bank closed its doors all of the bonds in question were in the files of the Bank and the notes secured thereby were unpaid in substantial amounts. The depositors of the bank have suffered severe loss (R. 60) and many of the deposits were made after the fraudulent execution of the bonds and the reliance thereon by the examiners and Comptroller of the Currency (R. 59).

Specification of Errors.

The Circuit Court of Appeals for the First Circuit erred in ruling:

(1) That all defenses available against a national bank are available against its receiver after the bank has become insolvent, on the theory that such receiver stands no better than the bank itself.

(2) That since Ragan (the Bank's president) knew that Cliff (the Surety Company's agent) was acting in fraud of his principal and violating the latter's instructions in executing the bonds, such knowledge on Ragan's part is to be imputed to the Bank with the result that the Receiver cannot recover on the bonds.

(3) That no estoppel arises in favor of the receiver, even though: (a) Cliff's written and publicly disclosed power of attorney included authority to write bonds of this type; (b) he gave said bonds with the intent that they should appear to be valid and enforceable obligations of the Surety Company in favor of the Bank; (c) he intended that the bonds should be shown to the bank examiners, bank directors and

other interested persons, and relied upon by them as valid obligations of his principal; (d) the duplicate originals of Cliff's power of attorney were furnished to him by the Surety Company for the purpose of having them shown or delivered to third parties dealing with Cliff as proof of his unlimited authority; (e) the bank examiners saw and relied upon the bonds and the power of attorney; (f) the bank examiners failed to seasonably discover the unsound and eventually insolvent condition of the Bank because of such reliance; and (g) the Bank's depositors and other creditors suffered loss because of such reliance.

Summary of Argument.

The Circuit Court of Appeals has held that a receiver of an insolvent national bank cannot recover on obligations held by the bank, which were given to the bank for the purpose of having the same appear to be sound, valid and enforceable obligations, because such obligations were given to the bank under such circumstances that the bank itself could not have recovered thereon had it continued as a going concern.

The petitioners do not admit that Ragan's knowledge can be imputed to the bank so as to have prevented it from recovering on the "note-guaranty bonds" if it had continued as a going concern. However, assuming that point for purposes of argument, the petitioners contend that in ruling that a receiver stands no better than the bank the Circuit Court of Appeals for the First Circuit erroneously construed language contained in decisions of this Court as establishing the rule which it applied, and disregarded decisions of this Court which recognize that the rights of a receiver under certain circumstances are greater than those of the bank. The conflict of opinion between the several Circuit Courts of Appeals and between the highest courts of the several states together with the public importance of the question presented warrants a review by this Court.

ARGUMENT.

I.

This Honorable Court Has Never Held that a Receiver of an Insolvent National Bank Cannot Recover on Obligations Held by the Bank, Which Were Given to the Bank for the Purpose of Having the Same Appear to be Sound, Valid and Enforceable Obligations, Simply Because the Obligations Were Given to the Bank Under Such Circumstances that the Bank Itself Could Not Have Recovered Thereon Had It Continued as a Going Concern.

The case of *Scott* v. *Armstrong,* 146 U. S. 499; 36 L. Ed. 1059 (1892) contains a statement as to the status of the receiver of a national bank, which appears to have been relied upon by the court below as stating a general and all-inclusive rule of law applicable to receivers of national banks. This dictum at p. 507 reads as follows:

> "* * * The receiver took the assets of the Fidelity Bank as a mere trustee for creditors, and not for value and without notice, and, in the absence of statute to the contrary, subject to all claims and defenses that might have been interposed as against the insolvent corporation before the liens of the United States and of the general creditors attached."

A study of the decision discloses that this language was wholly sound as applied to the facts and issues in that case, but it was used in an opinion which dealt only with the right of set-off with respect to debits and credits in settling the claim of a depositor in a closed bank. No questions of fraud practiced on the bank or of intention to deceive the bank examiners, the depositors or the public, were involved. It is respectfully submitted that in using the above quoted language the Court was not attempting to state a general principle of law applicable to receivers of national banks covering all circumstances.

The case of *Rankin, Receiver*, v. *City National Bank*, 208 U. S. 541; 52 L. Ed. 610 was also relied upon by the Circuit Court of Appeals for the First Circuit as being decisive in the cases at bar.

In that case a bank examiner had complained of excessive loans made by the Guthrie Bank. Billingsley, president of the said bank, advised the cashier of the City Bank of this fact and requested that the City Bank take his personal note and credit the Guthrie Bank with the proceeds under an agreement that the proceeds would be kept in a special account not subject to check and available at all times for offset against the note. The credit thus established in favor of the Guthrie Bank enabled it to eliminate the excessive loans. Subsequently, but before the closing of the Guthrie Bank, the note was charged against the special account by the City Bank as per agreement. The Receiver of the Guthrie Bank sued the City Bank on the theory that the special account was an asset of the Guthrie Bank and not subject to offset against the note of Billingsley. It will be observed that the transaction between the two banks had been fully closed by the offsetting of the note against the special account in the name of the Guthrie Bank in strict conformity with the agreement made between Billingsley and the City Bank and in so far as the City Bank was concerned the arrangement was not in furtherance of any conspiracy to defraud the Guthrie Bank.

In that case Mr. Justice Holmes speaking for the Court said at p. 546:

> "* * * If the Guthrie Bank had sued while it was a going concern it could not have recovered, and the receiver stands no better than the bank."

It is submitted that in using this language Mr. Justice Holmes did not intend that the words should be construed other than as applicable to the particular facts of the case under consideration.

A careful reading of the decision in the Rankin case shows that none of those special elements of fact were

present which are the basis of those decisions which favor the Receiver's position in the cases at bar, so that there was no occasion for the Court to consider the legal effect of the giving of an obligation to a bank with the **intention on the part of the maker** that it should be used for the purpose of exhibition to the bank examiners and directors, to the end that they might regard it as a sound and enforceable obligation securing an asset of the bank. There is not the slightest indication in the Rankin case that the existence of the credit supplied by the defendant City Bank in any way operated to keep the Guthrie Bank open for any period of time. It is significant to note that in contrast to the instant case no one was injured by the transaction with the City Bank because the notes representing the excessive loans remained the property of the Guthrie Bank. Any loss thereon was sustained prior to the transaction with the City Bank. In the instant case the granting of the loans and the original approval thereof by the directors of the bank was based upon the fraudulent transactions of Ragan and Cliff.

It is submitted, therefore, that the Rankin case is not an authority for the general proposition of law for which it appears to have been cited by the Circuit Court of Appeals for the First Circuit and is, in fact, inapplicable to the cases at bar.

The Circuit Court of Appeals also cited in support of its ruling above referred to the case of *Fourth Street National Bank* v. *Yardley*, 165 U. S. 634; 41 L. Ed. 855. That case held that where an equitable lien upon certain assets of an insolvent national bank existed prior to the closing of the bank the receiver took the assets subject to the lien. No question was involved of intent to deceive the bank examiners or to give the bank an obligation which appeared to be enforceable but was coupled with an understanding that it would not be enforced, and, therefore, the case is not applicable to the questions of law presented in the instant case.

II.

This Honorable Court Has Decided that a Receiver of a National Bank Has Certain Rights With Respect to Third Parties Superior to the Rights of the Bank Itself.

In the case of *Texas & Pacific Railway Co.* v. *Pottorff, Receiver,* 291 U. S. 245; 78 L. Ed. 777 (1934), it was held that a depositor could not enforce against the receiver of a national bank a contract under which the bank had agreed to segregate certain of its securities and hold the same as collateral to secure the repayment of the customer's deposit. In that case the receiver was held not to be bound by the agreement as to security and the depositor was left in the position of an unsecured creditor of the bank. This Court speaking through Mr. Justice Brandeis therein stated at page 260:

> "But even if the bank would have been estopped from asserting lack of power, its receiver would be free to challenge the validity of the pledge. The unauthorized pledge reduced the assets available to the general creditors. It is the duty of the receiver of an insolvent corporation to take steps to set aside transactions which fraudulently or illegally reduce the assets available for the general creditors, even though the corporation itself was not in a position to do so.
> "* * * The receiver may assert the invalidity of the pledge without making restitution by paying the pledgee's claim in full."

See also *City of Marion* v. *Sneeden, Receiver,* 291 U. S. 262; 78 L. Ed. 787 (1934).

This court has held that stockholders of defunct national banks are liable for the payment of stock assessments, even though their shares had been purchased in reliance upon grossly fraudulent misrepresentations as to the condition of the banks made by officers of the banks for the purpose of inducing the stockholders to purchase shares from the banks. See *Scott* v. *Dewecse, Receiver,* 181 U. S. 202, 213;

45 L. Ed. 822 (1901), and *Lantry* v. *Wallace, Receiver,* 182 U. S. 536, 550, 551; 45 L. Ed. 1218 (1901). In each of those cases the bank itself was the vendor of the stock and the fraudulent misrepresentations were made by officers of the bank who had been duly authorized to sell the shares in question. As a result of the decision in those two cases the receivers were held entitled to enforce, for the benfit of the banks' creditors, obligations which were imposed upon these stockholders as a result of the fraudulent acts of the banks' own officers. Also see *Oppenheimer* v. *Harriman National Bank and Trust Company,* 301 U. S. 206, 81 L. Ed. 663, 667.

This Court has recently held that the receiver of a private corporation (as distinguished from a national banking association) may recover from fraudulent promoters and that in so recovering the receiver acts as the representative and for the benefit of the creditors of the corporation. See *McCandless* v. *Furlaud, et al.,* 296 U. S. 140, 160; 80 L. Ed. 121 (1935).

The decision in that case appears to be an express recognition of the legal principle that where fraud is involved a receiver, acting as the representative of creditors and for their benefit, may enforce rights which the corporation itself could not have enforced.

III.

There is a Conflict of Authority Between the Federal Courts of the Several Circuits With Respect to the Question of Whether a Receiver of an Insolvent National Bank May Recover on Obligations Held by His Bank Upon Which the Bank Itself, as a Solvent Going Concern, Could Not Have Recovered.

The conflict of opinion is reflected not only in the decisions of the several Circuit Courts of Appeals but also in the decisions of United States District Courts. It has, therefore, been deemed advisable to present the conflict of opinion by discussing sequentially the group of

cases which appear to support the position taken by the respondents including the cases relied upon by the Circuit Court of Appeals for the First Circuit and then the group of cases which sustain the position taken by the petitioners under the following headings:

A. *Discussion of the decisions of the Federal Courts which appear to support the position taken by the respondents, including the decisions cited by the Circuit Court of Appeals in the cases at bar.*

The Circuit Court of Appeals cited *Cutler* v. *Fry*, 240 Fed. 238 (D. C. Kan.) (1915); *Yates Center National Bank* v. *Schaede*, 240 Fed. 240 (D. C. Kan.) (1915); *Yates Center National Bank* v. *Lauber*, 240 Fed. 237 (D. C. Kan.) (1915). These cases were all decided by the same court on the same day and appear to rest upon the court's interpretation of the case of *Rankin* v. *City National Bank, supra.* Judge Pollock who wrote the opinions expressed reluctance that he must come to such a conclusion. He recognized the existence of the contrary doctrine, as laid down in the case of *Pauly* v. *O'Brien*, 69 Fed. 460, but appears to have felt compelled to deny the receiver the right to recover because of the holding of the Rankin case. The rationale of Judge Pollock's decision appears to be that the receiver cannot have the benefit of a promise contained in a note without assuming the burden of the bank's counter-promise that the note will not be enforced.

Since the decisions in these three District Court cases, however, this Honorable Court has decided that a receiver may have the benefits of a contract without assuming its burdens. See *Texas & Pacific Railway Co.* v. *Pottorff, Receiver, supra,* and *City of Marion* v. *Sneeden, supra.*

The case of *Skud* v. *Tillinghast, Receiver*, 195 Fed. 1 (C. C. A. 6) (1912) also cited by the Circuit Court of Appeals does not definitely lay down the broad rule of law which the Circuit Court of Appeals in the cases at bar appeared to assume to be a uniform rule in the Federal

Courts. Furthermore, in reaching its decision the court stated that it did not appear that Skud, the maker of the note, acted with any fraudulent intent or had in any way connived with the officers of the bank in any wrongdoing.

The case of *Peterson* v. *Tillinghast, Receiver,* 192 Fed. 287 (C. C. A. 6) (1911) was also cited by the Circuit Court of Appeals in the cases at bar. In this case Peterson had given his note payable to the bank at the request of an officer of the bank upon the express understanding that it was given for the accommodation of the bank and was to be used only for discounting at another bank to raise funds for the accommodated bank. The accommodated bank did not discount it, but held the note, which was in its possession when the receiver took over the bank's affairs. While the Rankin case is cited as laying down a rule of general application respecting the rights of a receiver of a national bank, it is clear that the decision really turns on the law of negotiable instruments. Inasmuch as the bank, as the accommodated payee of the note, never negotiated it to a third party, the maker could not be held liable thereon to the accommodated payee. It was expressly found that Peterson, the maker, gave the note in good faith and with no intent to deceive or aid in any fraud.

The Circuit Court of Appeals also cited as authority for its ruling the cases of *Burrowes* v. *Nimocks,* 35 F. (2) 152 (C.C.A. 4) (1929) and *Schumacher* v. *Eastern Bank & Trust Co.,* 52 F. (2) 925 (C.C.A. 4) (1931). Both of these cases dealt with the question of whether the receiver of a national bank was bound by an agreement with a depositor whereby the bank gave collateral to secure a loan or deposit. In the Schumacher case the court found as a fact that the transaction between the defunct bank and the defendant bank (Eastern Bank & Trust Co.) involved a loan and not a deposit, and held that the defunct bank had a right to pledge its assets to secure the loan. In the Burrowes case the defunct bank had pledged certain of its assets to secure a deposit of county funds. The court held

that in so doing the officials of the defunct bank acted within their legal authority and that since the bank itself was bound by its agreement with its depositor, the receiver likewise was bound.

Both of those cases were decided prior to the year 1934, when this Honorable Court decided the cases of *Texas & Pacific Railway Co.* v. *Pottorff, Receiver, supra,* and *City of Marion* v. *Sneeden, Receiver, supra,* which held that where a national bank has no authority to pledge its assets to secure a deposit, a receiver of the bank may reclaim the collateral and leave the depositor in the position of an unsecured creditor. Therefore, the above decisions of the Circuit Court of Appeals for the Fourth Circuit have been overruled in principle in so far as they held that a receiver's rights are no greater than those of his bank.

The case of *Keyes* v. *First National Bank of Aberdeen,* 20 F. (2) 678 (D. C. S. D.) (1927) also cited by the Circuit Court of Appeals, appears to turn on its particular facts which are in no way comparable to the facts in the cases at bar and do not involve the question of law here under consideration.

The decisions in the following cases (not cited by the Circuit Court of Appeals in the cases at bar) appear to hold to the view of law entertained by the Circuit Court of Appeals for the First Circuit; *Hookway* v. *First National Bank,* 36 F. (2) 166 (C.C.A. 8) (1929), *Andresen* v. *Kaercher,* 38 F. (2) 462 (C.C.A. 8) (1930), *Kaercher* v. *Citizens' National Bank,* 57 F. (2) 58 (C.C.A 8) (1932), and *Bosworth* v. *Cady,* 72 F. (2) 62 (C.C.A. 7) (1934).

It is of importance to note that all of the above decisions were rendered in the Sixth, Seventh and Eighth Circuits, and that the highest state courts of Kansas, Nebraska, North Dakota, Minnesota, Missouri, Kentucky, Ohio, Illinois and Wisconsin, (which States were embraced in said circuits at the time the above decisions were rendered) have all adopted the rule of law contended for by the petitioners.

B. *Discussion of Decisions of Federal Courts which sustain the Petitioners' contentions in the cases at bar.*

The earliest Federal case sustaining the petitioners' position is *Pauly* v. *O'Brien*, 69 Fed. 460 (C. C. Calif.) (1895). In that case it was held that the receiver of a national bank could recover on a promissory note which the maker had given to the bank to take the place of a note, the maker of which had become insolvent. The bank did not surrender the insolvent's note, but carried it as collateral to the defendant's note. The defendant pleaded no consideration. The court said (pp. 461, 462):

> "It will never do for the courts to hold that the officers of a bank, by the connivance of a third party, can give to it the semblance of solidity and security, and, when its insolvency is disclosed, that the third party can escape the consequences of his fraudulent act."

The doctrine contended for by the petitioners has been upheld in the Fourth Circuit in the case of *Federal Reserve Bank* v. *Crothers*, 289 Fed. 777 (C.C.A. 4) (1923). In that case a defendant executed a note to the bank at the solicitation of one Warburton, its president, who told the defendant that it was to be used to take the place of an equivalent principal amount of bonds of an electric light company owned by the bank, to which the bank examiners had objected. Warburton actually used the note in substitution for a note of a third party, which had been previously obtained by Warburton for the same ostensible purpose. Crothers received no consideration for the note and there was no evidence that the bank parted with anything in exchange for the note. The Circuit Court of Appeals for the Fourth Circuit ruled that the District Court should have instructed the jury to find for the plaintiff (the receiver of the bank). Mr. Circuit Justice Taft (then Chief Justice of this Honorable Court) sat on the case in the Circuit Court of Appeals as Circuit Justice and concurred in the opinion. In its opinion the court said:

> "Public policy requires that the maker be estopped from denying his liability under such circumstances."

A similar view of the law was taken by the Circuit Court of Appeals for the Fifth Circuit in the case of *Bohning* v. *Caldwell,* 10 F. (2) 298 (C.C.A. 5) (1925) Cert. Den. 271 U. S. 663, 70 L. Ed. 1139. This decision is of particular significance, inasmuch as in the course of the opinion the court referred to the case of *Pauly* v. *O'Brien, supra,* as stating the sound doctrine and also referred to the line of cases typified by the case of *Peterson* v. *Tillinghast, supra,* as appearing to hold the contrary view. The court held that the receiver could recover and as noted above this Honorable Court denied certiorari.

See also *Utley* v. *Clarke, et al.,* 16 Fed. Supp. 435 (D. C. N. D. N. Y.) (1936) which also adopted the view of the law here contended for by petitioners, after a review of the authorities on both sides of the question. In that case the court expressed itself as follows on page 439:

> "While, if the bank were solvent and a going concern, plaintiff might recover, he cannot recover when he has been party to a deception upon the depositors and creditors of the bank and upon the Comptroller of the Currency when the bank becomes insolvent and his securities are taken by the receiver. He is estopped from asserting his claim as against depositors and other creditors."

From the foregoing it appears that there is a direct conflict of opinion in the several circuits on this important question and that the decision of the Circuit Court of Appeals for the First Circuit in the cases at bar has increased the existing confusion.

IV.

The Overwhelming Weight of Opinions of the State Courts Favors the Position Contended for by the Petitioner and is in Conflict With the Ruling of the Circuit Court of Appeals in the Cases at Bar.

The decisions in the following State Court cases adopt the rule of law here contended for. Those appearing in bold type contain particularly clear and persuasive statements of the rule.

ALABAMA: See *Day* v. *Farmers' & Merchants' Bank*, 229 Ala. 372, 376-377, 157 So. 439, 443-444 (1934)

COLORADO: **Murphy, Receiver** v, **Gumaer**, 18 Colo. App. 183, 70 Pac. 800, 802-803 (1902).

FLORIDA: *Ashley* v. *Rowe*, 101 Fla. 110, 133 So. 551, 552 (1931).

ILLINOIS: *Golden* v. *Cervenka*, 278 Ill. 409, 116 N. E. 273, 282, 283, (1917); *Niblack* v. *Farley*, 286 Ill. 536, 122 N. E. 160 (1919); *Boller* v. *Field*, 260 Ill. App. 488, 492 (1931); *Nelson* v. *Colegrove*, 265 Ill. App. 488 (1932).

KANSAS: *German-American State Bank* v. *Watson*, 99 Kan. 686, 163 Pac. 637 (1917); **Cedar State Bank** v. **Olson**, 116 Kan. 320, 226 Pac. 995, 997 (1924); *Hayes* v. *Addy*, 139 Kan. 481, 32 Pac. (2) 243, (1934); *Bell* v. *Johnson*, 142 Kan. 360, 46 Pac. (2) 886, (1935).

KENTUCKY: *Denny* v. *Fishter*, 238 Ky. 127, 36 S. W. (2) 864, (1931).

MARYLAND: See *New* v. *Page*, 144 Md. 606, 125 Atl. 403, 404. (1924)

MASSACHUSETTS: **Prudential Trust Co.** v. **Moore**, 245 Mass. 311, 139 N. E. 645, 647 (1923).

MINNESOTA: *Skordal* v. *Stanton*, 89 Minn. 511, 95 N. W. 449 (1903); **German-American Finance Corp.** v. **Merchants & Mfrs. Bank**, 177 Minn. 529, 225 N. W. 891, 893 (1929).

MISSOURI: *Third National Bank of St. Louis* v. *Reichert*, 101 Mo. App. 242, 73 S. W. 893, 896 (1903).

MONTANA: *State Bank of Moore* v. *Forsyth*, 41 Mont. 249, 108 Pac. 914, 919 (1910).

NEBRASKA: *Harrington* v. *Connor*, 51 Neb. 214, 70 N. W. 911 (1897).

NEW JERSEY: See *Schmid* v. *Haines*, 115 N. J. L. 271, 274, 178 Atl. 801, 803 (1925).

NEW YORK: **Hurd** v. **Kelley**, 78 N. Y. 588 (1879); **Best** v. **Thiel**, 79 N. Y. 15 (1879); *Sickles* v. *Herold*, 32 N. Y. S. 1083, 1085 (1895); **Bay Parkway Nat. Bank** v. **Shalom**, 270 N. Y. 172, 200 N. E. 685, 687 (1936).

NORTH DAKOTA: *Vallely* v. *Devaney*, 49 N. Dak. 1107, 194 N. W. 903, (1923); *Peterson* v. *Baird*, 63 N. Dak. 604, 249 N. W. 690 (1933).

OHIO: *State, ex rel. Lattanner* v. *Hills*, 94 Ohio St. 171, 113 N. E. 1045, 1047 (1916).

OKLAHOMA: *First National Bank* v. *Boxley*, 129 Okla. 159, 264 Pac. 184, 187 (1927).

OREGON: *Putnam* v. *Chase*, 106 Ore. 440, 212 Pac. 365 (1923).

PENNSYLVANIA: *State Bank of Pittsburg* v. *Kirk*, 216 Pa. 452, 65 Atl. 932; (1907); **Lyons** v. **Benney**, 230 Pa. 117, 79 Atl. 250, 251; (1911); *Warren National Bank* v. *Jamieson*, 301 Pa. 45, 151 Atl. 672; (1930).

SOUTH CAROLINA: **Arthur** v. **Brown**, 91 S. Car. 316, 74 S. E. 652, 654, (1912).

TEXAS: **Shaw** v. **Borchers**, 46 S. W. (2) 967, 969, 970, (Tex. Civ. App. (1932)).

UTAH: See *Riches* v. *Hadlock*, 80 Utah 265, 288, 15 Pac. (2) 283, 292, (1932).

VERMONT: *West Rutland Tr. Co.* v. *Houston*, 104 Vt. 204; 158 Atl. 69, 71-72 (1932).

VIRGINIA: See *Webb* v. *Pleasants*, 144 Va. 516, 519; 132 S. E. 175, 176 (1926).

WASHINGTON: *Moore* v. *Kildall*, 111 Wash. 504; 191 Pac. 394 (1920).

WISCONSIN: *Schwenker* v. *Teasdale*, 206 Wisc. 275, 239 N. W. 434, 437-438 (1931).

See also: *Allen* v. *Hay,* 64 Can. S. C. 76; 69 Dom. L. R. 193 (1922); (Note) 38 Harvard Law Review, 239; (Anno.) 64 A.L.R. 595, 601-605.

V.

Sound Public Policy Demands the Protection of Depositors and Creditors of Banking Institutions and the Public from Frauds Such as Are Involved in these Cases.

National Banks are governmental instrumentalities, *M'Culloch* v. *State of Maryland,* 17 U. S. 316, 436, 437; 4 L. Ed. 579 (1819), *Osborn* v. *Bank of the United States,* 22 U. S. 739, 861, 6 L. Ed. 204 (1824), and, therefore, the business of such banks is impressed with a public interest. See *German American Finance Corporation* v. *Merchants and Manufacturers Bank,* 177 Minn. 529, 225 N. W. 891, 893.

Consistent with the holdings of the courts in the above cases Congress has seen fit to take definite steps for the protection of the interests of the depositors of national banks and the public by reposing in the Comptroller of the Currency supervisory control over national banks under statutory provisions which prescribe certain restrictions and requirements. Among other things, each national bank must submit regular reports to the Comptroller disclosing the condition of the bank (12 U. S. C. 161), and all such banks are subject to examination by examiners of the Comptroller's office (12 U. S. C. 481).

If the Comptroller becomes satisfied of the insolvency of a national bank he may appoint a receiver and liquidate the assets thereof for the benefit of its creditors (12 U. S. C. 191).

In addition, Congress has imposed a duty upon the Comptroller to report to it any suggestions he may have relative to banking by which the system may be improved and by which the **"security of the holders of its notes and other creditors may be increased."** (12 U. S. C. 14). The

quoted phrase indicates a disposition on the part of Congress to regard national banks as so affected with a public interest as to require special measures for the protection of their creditors and the public.

These statutory sections are for the primary protection of the depositors and the public and are founded in a sound public policy. *United States National Bank of La Grande* v. *Pole,* 2 F. Supp. 153, 157 (D. C. Oregon) (1932).

As aforenoted, one of the methods employed by the sovereign to protect the interests of the public and depositors of national banks is by examinations made by the Comptroller through his examiners. Any rule of law which permits third persons to escape liability to the depositors and creditors of a bank (or a receiver acting for their benefit), where such persons have conspired with fraudulent bank officials to deceive the Comptroller, his examiners, and through them the public (and have in fact caused a loss to be sustained by the bank's creditors), by placing among the assets of the bank obligations prima facie valid and enforceable but concerning which the liability has been limited or voided by private secret agreement between the conspirators, defeats the entire purpose of the regulatory statutes and is in conflict with a sound public policy.

CONCLUSION.

The petitioners therefore respectfully submit that a writ of certiorari should issue as prayed for.

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